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IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 26.2.2007

CORAM

THE HON'BLE MR.JUSTICE P.D.DINAKARAN
AND
THE HON'BLE MRS.JUSTICE CHITRA VENKATARAMAN

T.C.(A).Nos.22, 196 and 466 of 2004

Commissioner of Income Tax II,
Trichy. .. Appellant

Vs.

M/s.City Union Bank Ltd.,
Kumbakonam. .. Respondent

Prayer in TC.[A] No.22/2004: Appeal under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'B' Bench dated 18.6.2003 made in ITA No.2483/Mds/1995 for the assessment year 1992-93 and against the order of the commissioner of Income Tax [Appeals] VI Madras 600 034 in ITA.No.113/95-96/D.O.Spl.R.Try dated 9.9.1995 and against the Order dated 28.3.1995 in PAN/GIR.No.0349 of the Deputy Commissioner of Income Tax, special Range, Tiruchirappalli.

Prayer in TC[A].No.196/2004: Appeal under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'C' Bench dated 5.11.2003 made in ITA No.1341/Mds/1995 for the assessment year 1991-92 and against order dated 31.3.1995 in ITA.No.622/93-94/Try of the Commissioner of Income Tax [Appeals] VI, Madras and against the order dated 10.1.1994 in PAN/GIR NO.CN-0349 of the Deputy Commissioner of Income Taxx, Special Range, Tiruchirappalli.

Prayer in TC[A].No.466/2004: Appeal under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'B' Bench dated 5.8.2003 made in ITA No.2159/Mds/1996 for the assessment year 1993-94 and against Order of the Commissioner of Income Tax [Appeals] VI Madras in ITA.No.256/96-97/DL.Spl.TRY dated 9.7.96 and against the order dated 22.3.1994 in PAN/GIR No.CN-0349 of the Deputy Commissioner of Income Tax Special Range, Tiruchirappalli.

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For Appellant : Mr.Muralikumaran
Senior Standing Counsel (IT)

For Respondent : Mr.V.D.Gopal

J U D G M E N T

(Delivered by P.D. DINAKARAN, J.)

The above tax case appeals were admitted on the following questions of law:

T.C.(A) No.22 of 2004

1. Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that in the case of the assessee bank interest on securities has to be assessed only on the basis of the interest due on the half-yearly due dates and the interest accrued as at the end of the assessment year is not be taken?
2. Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the claim of bad debts in relation to non-rural branches of the assessee bank is allowable without first setting off against the provision already allowed under Section 36(1)(viia) when no distinction is made between advances relating to non-rural and rural advances has been made in Section 36(1)(vii)?
3. Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the reduction of Rs.47,38,984/- claimed by the assessee bank as diminution in the value of investments is allowable when the loss has been claimed only on notional basis in the adjusted statement filed along with the return of income and not on the basis of any definite method of accounting followed in the books of accounts?

T.C.(A) No.196 of 2004

1. Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the claim of bad debts in relation to non-rural branches of the assessee bank is allowable without first setting off against the provision already allowed under Section 36(1)(viia), when no distinction is made between advances relating to non-rural and rural advances has been made in Section 36(1)(vii)?

T.C.(A) No.466 of 2004:

1. Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that in the case of the assessee bank interest on securities has to be assessed only on the basis of the interest due on the half-yearly due dates and the interest accrued as at the end of the assessment year is not be taken? and

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2.Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the claim of bad debts in relation to non-rural branches of the assessee bank is allowable without first setting off against the provision already allowed under Section 36(1)(viia), when no distinction is made between advances relating to non-rural and rural advances has been made in Section 36(1)(vii)?

2.1. The Assessing Officer observing that interest on securities was to be assessed in accordance with the method of accounting regularly employed by the assessee, and as the assessee was following accrual basis for recording interest in the books of accounts, included the interest on accrual basis for computing the total income.

2.2. With regard to the claim of the assessee qua bad debts written off, the Assessing Officer observing that as per the proviso to Section 36 (1)(viia) of the Act, any bad debt in excess of the provision has to be disallowed and the section does not distinguish the debt that is arising from urban advances and rural advances, rejected the stand of the assessee that the provision referred to in Section 36(1)(viia) relates to only the rural branches and does not apply to bad debts of urban branches, and held that the actual bad debts irrespective of the question as to whether they are related to urban or rural branches should be first set off against the provision which has already been allowed and only the excess should be allowed to be deducted under Section 36(1)(vii) of the Act.

2.3. Apropos the claim of the assessee with regard to diminution in the value of investments written off, the assessing officer declined to allow the claim on the ground that a reference application on this issue was pending before this Court.

2.4. On appeals filed by the assessee, the Commissioner of Income Tax (Appeals), held in favour of the assessee, which was on further appeal, at the instance of the Revenue, confirmed by the Tribunal. Hence, these appeals raising the questions of law referred to above.

3. Heard both sides.

4.1. With regard to the first substantial question of law raised in T.C.(A) No.22 of 2004 and the first substantial question of law raised in T.C.(A) No.466 of 2004, the Division Bench of this Court by judgment dated 23.1.2007 made in T.C.(A) Nos.15 and 24 of 2003 (Commissioner of Income Tax, Madurai v. Tamilnadu Mercantile Bank Ltd., Tuticorin), after referring to the decisions in Commissioner of Income-tax v. Canara Bank [1992] 195 ITR 66, CIT v. Shoorji Vallabhdas and Co. [1962] 46 ITR 144, H.M.Kashiparekh and Co. Ltd. v. CIT [1960] 39 ITR 706, Poona Electric Supply Co. Ltd. v. CIT [1965] 57 ITR 521, Morvi Industries Ltd. v. CIT, [1971] 82 ITR 835, State Bank of Travancore v. CIT [1986] 158 ITR 102

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(SC), Godhra Electricity Co. Ltd., v. Commissioner of Income-tax, [1997] 225 ITR 746 held that the assessee is taxable for interest on securities only on specified dates when it becomes due for payment, in view of third proviso to Section 145(1) of the Act, which was in force during the relevant assessment years.

4.2. In view of the ratio laid down in the decisions referred supra, the first substantial question of law raised in T.C.(A) No.22 of 2004 and the first substantial question of law raised in T.C.(A) No.466 of 2004 is answered in favour of the assessee and against the revenue.

5.1. With regard to the second question of law in T.C.(A) No.22 of 2004, the only question of law in T.C.(A) No.196 of 2004 and the second question of law in T.C.(A) No.466 of 2004, the learned counsel for the assessee submitted that a similar issue has been answered in favour of the assessee in South Indian Bank Ltd. v. Commissioner of Income-tax, [2003] 262 ITR 0579.

5.2. The Division Bench of Kerala High Court in South Indian Bank Ltd. Case referred supra, held that:

> "The proviso to clause (vii) of section 36(1) and clause (v) of section 36(2) of the Income-tax Act, 1961, were inserted simultaneously with effect from April 1, 1985, by the Finance Act, 1985. The scope of the proviso to clause (vii) of section 36(1) has to be ascertained from a cumulative reading of the provisions of clauses (vii), (viia) of section 36(1) and clause (v) of section 36 (2). The intention of the Legislature in enacting the proviso to clause (vii) of section 36(1) and clause (v) of section 36(2) simultaneously is only to see that a double benefit in respect of the same bad debt is not given to a scheduled bank. A scheduled bank may have both urban and rural branches and advances given from both branches. Having regard to the hazards involved in realising the advances made by rural branches particularly to agriculturists, certainly the assessee-bank might prefer to make provision for bad debt in respect of advances made in the rural branches. As a result of the amendment the scheduled bank will be entitled to the deduction of the entire bad debt relating to advances made by the urban branches written off in the books and also the difference between the amount written off in the books relating to advances made by the rural branches during the previous year relevant to the assessment year and the credit balance in the provisions for bad and doubtful debts account relating to advances made by the rural branches made under clause (viia). If the bad debt written off relates to debts other than for which provision is made under clause (viia) such debt will fall squarely under the main part of clause (vii) which is entitled to deduction and in respect of that part of the debt with reference to which a provision is made under clause (viia), the proviso will operate to limit the deduction to the extent of the difference between that part of debt written off

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in the previous year and the credit balance in the provision for bad and doubtful debts account made under clause (viia)."

5.3. In the instant case, while allowing the claim for bad debts written off in respect of advances made by rural branches, the Commissioner of Income Tax (Appeals) as well as the Tribunal, was of the firm opinion that the assessee has not claimed any debts written off in respect of rural branch in the earlier year. If that be so, we find no error in the order of the Tribunal in holding that the claim of bad debts in relation to non-rural branches of the assessee bank is allowable. Accordingly, this issue is answered in favour of the assessee and against the Revenue.

6.1. Qua the third question of law in T.C.(A) No.22 of 2004 is concerned, the Tribunal held that when investments are made in accordance with the requirements of the Act, wherein the market price changed from the value shown in the opening balance and at the end of the year, the same could be allowed as depreciation.

6.2. That apart, it is a settled law that the assessee is entitled to change the method of valuation of Government securities to market value from cost, and claim depreciation on the difference, vide Commissioner of Income Tax v. Karur Vysya Bank Ltd., [2005] 273 ITR 510.

6.3. In view of the ratio enunciated from the decision referred supra, we find no infirmity in the decision of the Tribunal in this regard.

Resultantly, the appeals are dismissed. No costs.

Sd/-
Asst. Registrar.

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Sub Asst. Registrar.

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To:

1. The Assistant Registrar,
Income Tax Appellate Tribunal,
III Floor, Rajaji Bhavan,
Besant Nagar, Chennai.

2.The Commissioner of Income Tax-II, Tiruchirappalli.

3. The Commissioner of Income
Tax (Appeals)-VI, Madras.

4.The Deputy Commissioner of
Income Tax, Special Range
Tiruchirapalli.

+ 2 CCs to Mr.N.Muralikumaran, Advocate SR NO 12000, 12001

+ 1 CC To Mr. V.N.Gopal, Advocate SR NO.11673

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